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UNITED STATES DEPARTMENT OF AGRICULTURE
FARM CREDIT ADMINISTRATION
WASHINGTON, D. C.

SUMMARY OF CASES
RELATING TO
FARMERS' COOPERATIVE ASSOCIATIONS

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FULL-SUPPLY CONTRACTS HELD INVALID

In the case of the Standard Oil Company of California v. United States, 69 S. Ct. 1051, it was held that exclusive or full-supply contracts which the Standard Oil Company of California had entered into with retail sellers of gasoline, and under which the Standard Oil Company undertook to furnish these retail gasoline dealers with all the gasoline, or other petroleum products, or accessories which they might require, were invalid.

The trial court, in 78 F. Supp. 850, held that contracts of the type in question were invalid because they violated section 1 of the Sherman Act 1/ and also section 3 of the Clayton Act 2/. On appeal, the holding of the trial court was affirmed, except that the Supreme Court of the United States found it unnecessary to pass on the question of whether the contracts violated section 1 of the Sherman Act. The following quotations from the opinion of the Supreme Court show the basis for the conclusion reached:

> "Since sec. 3 of the Clayton Act was directed to prohibiting specific practices even though not covered by the broad terms of the Sherman Act, it is appropriate to consider first whether the enjoined contracts fall within the prohibition of the narrower Act. The relevant provisions of sec. 3 are:
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> "'It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities, whether patented or unpatented, for use, consumption, or resale within the United States * * * on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods * * * of a competitor or competitors of the * * * seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.'
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> "Obviously the contracts here at issue would be proscribed if sec. 3 stopped short of the qualifying clause beginning, 'where the effect of such lease, sale, or contract for sale * * *.' If effect is to be given that clause, however, it is by no means obvious, in view of Standard's minority share of the 'line of commerce' involved, of the fact that that share has not recently increased, and of the claims of these contracts to economic utility, that the effect of the contracts may be to lessen competition or tend to create a monopoly. It is the qualifying clause, therefore, which must be construed.

1/ 15 U.S.C. 1.
2/ 15 U.S.C. 14.

"The District Court held that the requirement of showing an actual or potential lessening of competition or a tendency to establish monopoly was adequately met by proof that the contracts covered 'a substantial number of outlets and a substantial amount of products, whether considered comparatively or not.' Given such quantitative substantiality, the substantial lessening of competition - so the court reasoned - is an automatic result, for the very existence of such contracts denies dealers opportunity to deal in the products of competing suppliers and exclude suppliers from access to the outlets controlled by those dealers. Having adopted this standard of proof, the court excluded as immaterial testimony bearing on 'the commercial merits or demerits of the present system as contrasted with a system which prevailed prior to its establishment and which would prevail if the court declared the present arrangement [invalid].' The court likewise deemed it unnecessary to make findings, on the basis of evidence that was admitted, whether the number of Standard's competitors had increased or decreased since the inauguration of the requirements-contract system, whether the number of their dealers had increased or decreased, and as to other matters which would have shed light on the comparative status of Standard and its competitors before and after the adoption of that system. The court concluded:

"'Grant that, on a comparative basis, and in relation to the entire trade in these products in the area, the restraint is not integral. Admit also that control of distribution results in lessening of costs and that its abandonment might increase costs. * * * Concede further, that the arrangement was entered into in good faith, with the honest belief that control of distribution and consequent concentration of representation were economically beneficial to the industry and to the public, that they have continued for over fifteen years openly, notoriously and unmolested by the Government, and have been practised by other major oil companies competing with Standard, that the number of Standard outlets so controlled may have decreased, and the quantity of products supplied to them may have declined, on a comparative basis. Nevertheless, as I read the latest cases of the Supreme Court, I am compelled to find the practices here involved to be violative of both statutes. For they affect injuriously a sizeable part of interstate commerce, or, - to use the current phrase - "an appreciable segment" of interstate commerce.'

"The issue before us, therefore, is whether the requirement of showing that the effect of the agreements 'may be to substantially lessen competition' may be met simply by proof that a substantial portion of commerce is affected or whether it must also be demonstrated that competitive activity has actually diminished or probably will diminish.

"Since the Clayton Act became effective, this court has passed on the applicability of sec. 3 in eight cases, in five of which it upheld determinations that the challenged agreement was violative of that Section. Three of these - United Shoe Machinery Corp. v. United States, 258 U.S. 451, 42 S. Ct. 363, 66 L. Ed. 708; International Business Machines Corp. v. United States, 298 U.S. 131, 56 S. Ct. 701, 80 L. Ed. 1085; International Salt Co. v. United States,

332 U.S. 392, 68 S. Ct. 12, 92 L. Ed. 20 - involved contracts tying to the use of a patented article all purchases of an unpatented product used in connection with the patented article. The other two cases - Standard Fashion Co. v. Magrane-Houston Co., 258 U. S. 346, 42 S. Ct. 360, 66 L. Ed. 653; Fashion Originators' Guild v. Federal Trade Comm'n, 312 U.S. 457, 61 S. Ct. 703, 85 L. Ed. 949 - involved requirements contracts not unlike those here in issue."

* * * * * * * * * *

"We are dealing here with a particular form of agreement specified by sec. 3 and not with different arrangements, by way of integration or otherwise, that may tend to lessen competition. To interpret that section as requiring proof that competition has actually diminished would make its very explicitness a means of conferring immunity upon the practices which it singles out. Congress has authoritatively determined that those practices are detrimental where their effect may be to lessen competition. It has not left at large for determination in each case the ultimate demands of the 'public interest,' as the English lawmakers, considering and finding inapplicable to their own situation our experience with the specific prohibition of trade practices legislatively determined to be undesirable, have recently chosen to do. Though it may be that such an alternative to the present system as buying out independent dealers and making them dependent employees of Standard Stations, Inc., would be a greater detriment to the public interest than perpetuation of the system, this is an issue, like the choice between greater efficiency and freer competition, that has not been submitted to our decision. We are faced, not with a broadly phrased expression of general policy, but merely a broadly phrased qualification of an otherwise narrowly directed statutory provision.

"In this connection it is significant that the qualifying language was added only after a flat prohibition of tying clauses and requirements contracts had passed both Houses of Congress. The conferees responsible for adding that language were at pains, in answering protestations that the qualifying clause seriously weakened the Section, to disclaim any intention seriously to augment the burden of proof to be sustained in establishing violation of it. It seems hardly likely that, having with one hand set up an express prohibition against a practice thought to be beyond the reach of the Sherman Act, Congress meant, with the other hand, to reestablish the necessity of meeting the same tests of detriment to the public interest as that Act had been interpreted as requiring. Yet the economic investigation which appellant would have us require is of the same broad scope as was adumbrated with reference to unreasonable restraints of trade in Chicago Board of Trade v. United States, 246 U.S. 231, 38 S. Ct. 242, 62 L. Ed. 683. To insist upon such an investigation would be to stultify the force of Congress' declaration that requirements contracts are to be prohibited wherever their effect 'may be' to substantially lessen competition. <u>If in fact it is economically desirable for service stations to confine themselves to the sale of the</u>

petroleum products of a single supplier, they will continue to do so though not bound by contract, and if in fact it is important to retail dealers to assure the supply of their requirements by obtaining the commitment of a single supplier to fulfill them, competition for their patronage should enable them to insist upon such an arrangement without binding them to refrain from looking elsewhere.

"We conclude, therefore, that the qualifying clause of sec. 3 is satisfied by proof that competition has been foreclosed in a substantial share of the line of commerce affected. It cannot be gainsaid that observance by a dealer of his requirements contract with Standard does effectively foreclose whatever opportunity there might be for competing suppliers to attract his patronage, and it is clear that the affected proportion of retail sales of petroleum products is substantial. In view of the widespread adoption of such contracts by Standard's competitors and the availability of alternative ways of obtaining an assured market, evidence that competitive activity has not actually declined is inconclusive. Standard's use of the contracts creates just such a potential clog on competition as it was the purpose of sec. 3 to remove wherever, were it to become actual, it would impede a substantial amount of competitive activity." (Underscoring added.)

In some of the exclusive contracts which the Standard Oil Company of California had entered into with retail dealers in gasoline, the retail dealers were specifically restricted from buying gasoline or other products from anyone else, but in other contracts the retail dealers were simply obligated to obtain all the gasoline or other products which they needed in their business from the Standard Oil Company of California. In some instances the contracts with the Standard Oil Company were oral, but in most cases they were in writing. "Of the written agreements, 2,712 were for varying specified terms; the rest were effective from year to year but terminable 'at the end of the first 6 months of any contract year, or at the end of any such year, by giving to the other at least 30 days prior thereto written notice.'"

In the underscored quotation given above from the opinion of the Supreme Court, it is assumed that service stations, if they find it economically desirable to confine themselves to the sale of petroleum products of a single supplier, will continue to obtain their petroleum products from such supplier, although they are not bound by contract to do so. The opinion of the Supreme Court, however, seems to foreclose an arrangement under which a service station could assure itself by contract that it will be able to obtain all the petroleum products which it requires in its business from a single supplier. The opinion leaves in doubt the question of whether, even for a brief period, a service station could contract with a supplier of petroleum products to furnish it with all of such products that it might require.

It has been suggested that possibly a contract which obligated a supplier to furnish a minimum amount of a commodity during a particular period of time, and fixed a maximum beyond which he would not be required to furnish such commodity, might be a means of solving the problem. It is questionable

however, if this is a sound approach, because if the minimum was fixed high enough, it could amount to a full-supply contract.

Four of the Justices of the Supreme Court vigorously dissented from the majority opinion. In the dissenting opinion of Mr. Justice Jackson, which was concurred in by the Chief Justice and Mr. Justice Burton, it is said:

> "It does not seem to me inherently to lessen this real competition when an oil company tries to establish superior service by providing the consumer with a responsible dealer from which the public can purchase adequate and timely supplies of oil, gasoline and car accessories of some known and reliable standard of quality. No retailer, whether agent or independent, can long remain in business if he does not always, and not just intermittently, have gas to sell. Retailers' storage capacity usually is limited and they are in no position to accumulate large stocks. They can take gas only when and as they can sell it. The Government can hardly force someone to contract to stand by, ever ready to fill fluctuating demands of dealers who will not in turn undertake to buy from that supplier all their requirements. And it is important to the driving public to be able to rely on retailers to have gas to retail. It is equally important that the wholesaler have some incentive to carry the stocks and have the transport facilities to make the irregular deliveries caused by varied consumer demands."

In the dissenting opinion of Mr. Justice Douglas, it is said:

> "It is common knowledge that a host of filling stations in the country are locally owned and operated. Others are owned and operated by the big oil companies. This case involves directly only the former. It pertains to requirements contracts that the oil companies make with these independents. <u>It is plain that a filling station owner who is tied to an oil company for his supply of products is not an available customer for the products of other suppliers. The same is true of a filling station owner who purchases his inventory a year in advance.</u> His demand is withdrawn from the market for the duration of the contract in the one case and for a year in the other. The result in each case is to lessen competition if the standard is day-to-day purchases. Whether it is a substantial lessening of competition within the meaning of the Anti-Trust Laws is a question of degree and may vary from industry to industry." (Underscoring added.)

No reason is apparent why the principle applied in the Standard Oil case would not be applicable to instances involving any commodities which suppliers were furnishing to distributors of such commodities. No full-supply or exclusive contract should be entered into without a full consideration of the question of whether a violation of the antitrust laws would result.

On April 27, 1948, the District Court of the United States for the District of Columbia dismissed the antitrust indictment against the Maryland & Virginia Milk Producers Association, and others. (See Summary No. 38, page 10.) The Government then appealed the case directly to the Supreme Court of the United States, but in United States v. Maryland & Virginia Milk Producers Association, Inc., et al., 335 U.S. 802, the Supreme Court directed that the case be heard by the United States Court of Appeals for the District of Columbia Circuit before it would pass upon the merits. On June 17, 1949, the United States Court of Appeals for the District of Columbia Circuit in an opinion as yet unreported reversed the District Court of the United States for the District of Columbia. The opinion of that Court is here given in full:

> "EDGERTON, J.: The government appeals from an order dismissing an indictment charging conspiracy to restrain trade in milk and milk products in the District of Columbia, and between the District and adjoining States, in violation of Sec. 3 of the Sherman Act, 26 Stat. 209, 15 U.S.C. 3. The government first appealed directly to the Supreme Court, which remanded the case to this court pursuant to 34 Stat. 1246, as amended, 18 U.S.C. 3731. United States v. Maryland & Virginia Milk Producers Assn., Inc., et al., 335 U.S. 802.
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> "The paragraphs of the indictment indicated by the figures in parentheses make substantially the following statements. The appellees are an incorporated Association, the members of which are about 1,500 Maryland and Virginia milk producers who supply 80 percent of the milk sold to distributors in the Washington metropolitan area (20); the Secretary-Treasurer of this Association (9); and seven corporations that distribute milk and its products to consumer and other purchasers in the District of Columbia. These distributors buy and resell 86 percent of all milk supplied to the Washington metropolitan area (21). Appellees have conspired to eliminate and suppress competition in the sale of milk to these distributors, in its purchase by them, and in its resale by them to consumers and other purchasers (35). For those purposes (36, 37) appellees have done these things. Appellee distributors have contracted with appellee Association that they will buy no milk from producers or others who are not members of the Association, but will buy only from the Association, as far as it is able to supply their needs, which it agrees to do as far as it can (36 (a) (b)). Appellees have agreed to fix the prices at which the distributors will buy milk (36 (g)) and also the prices at which they will resell it (36 (m)). They have agreed on a classification of milk for price purposes according to use (36 (f) (g)). They have agreed that appellee distributors will remove from the market 'excess' milk, i.e., any milk the Association has for sale in excess of the amount these distributors can resell at the prices agreed upon (36 (n) (o)). They have agreed that the Association will prevent and eliminate competition from distributors not parties to the conspiracy by inducing them not to cut prices, attempting to deprive price-cutters of adequate supplies of milk, interfering with the transportation of milk to them, furnishing milk

to appellee distributors at reduced rates for use in taking away contract business from price-cutters and driving them out of business (36 (p)). They have agreed that the Association will not supply milk to any distributor not agreeing to buy his full supply from the Association, at prices as low as those charged to appellee distributors (36 (d)). The conspiracy has been successful: 'The defendants by agreement and concerted action have done the things which, as hereinbefore alleged, they conspired to do.' (37)

"'Price-fixing agreements are unlawful per se under the Sherman Act and . . . no showing of so-called competitive abuses or evils which those agreements were designed to eliminate or alleviate may be interposed as a defense . . . . . If the so-called competitive abuses were to be appraised here, the reasonableness of prices would necessarily become an issue in every price-fixing case. In that event the Sherman Act would soon be emasculated; its philosophy would be supplanted by one which is wholly alien to a system of free competition . . . . . Any combination which tampers with price structures is engaged in an unlawful activity. Even though the members of the price-fixing group were in no position to control the market, to the extent that they raised, lowered, or stabilized prices they would be directly interfering with the free play of market forces. The Act places all such schemes beyond the pale . . .' Accordingly the government need not show or allege that prices have been 'raised and maintained at "high, arbitrary and non-competitive levels."' United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 218, 221, 222. 'Also it is unreasonable, per se, to foreclose competitors from any substantial market.' International Salt Co. v. United States, 332 U.S. 392, 396. Therefore 'full supply contracts', however legal they may be in other circumstances, cf. Pick Mfg. Co. v. General Motors Corp., 299 U.S. 3, are illegal when made for the purpose of eliminating and suppressing competition. Complete monopoly is of course unnecessary: 'the amount of interstate trade . . . affected by the conspiracy is immaterial in determining whether a violation of the Sherman Act has been charged in the complaint.' United States v. Yellow Cab Co., 332 U.S. 218, 225.

"Although the Capper Volstead Act, 42 Stat. 388, 7 U.S.C. 291, and the Clayton Act, 38 Stat. 730, 731, 15 U.S.C. 17, give some privileges to combinations of agricultural producers, <u>a combination of producers and distributors to eliminate competition and fix prices at successive stages in the marketing of an agricultural product is not privileged.</u> United States v. Borden Co., 308 U.S. 188; Allen Bradley Co. v. Local Union No. 3, U.S. 797, 808. 'Congress, as a part of its Agricultural Marketing Agreement Act, authorizes the Secretary of Agriculture to issue orders regulating the handling of several agricultural products, including milk . . . As to milk, it sets up subsection 8c (5) 7 U.S.C. subsection 608c (5), a rather complicated system of fixing prices to be paid to producers . . .' H. P. Hood & Sons v. Du Mond, 336 U.S. 525, 541. And the same Act, 50 Stat. 246, as amended,

7 U.S.C. 601 et seq., provides in subsection 608b (U.S.C. Supp. 1) that with certain limitations 'the Secretary of Agriculture shall have the power . . . to enter into marketing agreements with processors, producers, associations of producers, and others engaged in the handling of any agricultural commodity or product thereof' and 'The making of any such agreement shall not be held to be in violation of any of the antitrust laws of the United States, and any such agreement shall be deemed to be lawful.' But these provisions expressly involve orders of the Secretary of Agriculture and agreements to which he is a party. Since neither the fixing of prices according to use nor any other feature of the conspiracy charged in this indictment is covered by any such order or agreement, these statutory provisions are immaterial. United States v. Borden, supra, at 199-202. (Underscoring added.)

"In our opinion, therefore, the court erred in dismissing the indictment as not setting forth sufiicient facts to constitute a conspiracy in violation of the Sherman Act.

Reversed

"Wilbur K. Miller, J., dissents."

In considering the foregoing opinion it will be remembered that the Court was simply passing upon the question of whether the allegations of the indictment set forth a violation of section 3 of the Sherman Act. In other words, the Court simply held that as a matter of law the indictment charged an offense under the Sherman Act. It is understood that the defendants have applied for a writ of certiorari to the Supreme Court of the United States.

EXEMPTION LETTER

Thereefollows an unpublished ruling of the Bureau of Internal Revenue holding that an unnamed cooperative association continues to be eligible for exemption from the payment of Federal income taxes:

"April 21, 1949

"IT:P:ER
JJW

(Name of Cooperative Omitted)

Gentlemen:

"Reference is made to the evidence presented for use in determining your status for Federal income tax purposes at the present time. You were held to be entitled to an exempt status by Bureau ruling dated August 16, 1935.

"It is the opinion of this office, based upon the evidence presented, that you are operating so as to meet the requirements of a farmers' cooperative association within the purview of section 101(12) of the Internal Revenue Code. It is therefore held that the Bureau ruling of August 16, 1935, is still effective.

"Accordingly, <u>you will not be required to file income tax returns unless you change the character of your organization, the purposes for which you were organized, or your method of operation. Any such changes should be reported immediately to the collector of internal revenue for your district in order that their effect upon your exempt status may be determined. This requirement has particular reference (1) to your failure to keep accurate records of all business transacted with all patrons; (2) to the handling and marketing of products for nonmember patrons in an amount greater in value than the value of the products handled and marketed for members; (3) to the purchase of supplies and equipment for nonmembers in an amount greater in value than the value of the supplies and equipment purchased for members; (4) to the purchase of supplies and equipment for persons who are neither members or producers; (5) to your failure to carry out the distribution of patronage dividends to all member and nonmember patrons with that part of your net profits arising from business transacted with them which is set aside as part of your reserves or surplus, or which is used to pay off indebtedness on plant and equipment, and for other capital purposes; and (6) to the marketing of products furnished by nonproducers or the transaction of any business on other than a cooperative basis.</u>

"You will be required, however, to file annually an information return on Form 990 with the collector of internal revenue for your district so long as this exemption remains in effect. This form

may be obtained from the collector and is required to be filed on or before the fifteenth day of the fifth month following the close of your annual accounting period.

"The collector of internal revenue for your district is being advised of this action.

"This review of your status originated through an inquiry by you relative to the disposition of small patronage accounts. The treatment of these accounts will be made the subject of a separate communication.

"By direction of the Commissioner.

/s/ C. W. STOWE,
ACTING DEPUTY COMMISSIONER"

(Underscoring added.)

Particular attention is called to the fact that the cooperative receiving the letter given above is required to give notice to the Bureau of Internal Revenue if it makes any change in its organization, the purposes for which it was organized, or in its methods of operation. In this connection, there are given above six itemized propositions to which the requirement has particular reference.

ALLOCATIONS UNDER ONE DOLLAR

There follows an unpublished ruling of the Bureau of Internal Revenue relative to how allocations to patrons of less than $1.00 may be handled:

"May 25, 1949

"IT:P:ER
JJW

(Name of Cooperative Omitted)

Gentlemen:

"Reference is made to your letter of December 24, 1948, in which you request permission to transfer to your educational fund patronage accounts of less than $1.00. You state that in allocating your earnings for the fiscal year ended June 30, 1948, you found that it was necessary to make 236 allocations of earnings of less than $1.00; that the average amount of such accounts was less than 42 cents; and that the cost of allocating earnings for each patron is approximately 66 cents.

"It is the opinion of this office that where the expense of maintaining a patronage account of less than $1.00 is greater than the amount involved, you may eliminate the account and place the amount in your educational fund, without thereby affecting your present exempt status for Federal income tax purposes.

Very truly yours,

/s/ Deputy Commissioner"

In the case of Woods v. Interstate Realty Co., 69 S. Ct. 1235, it appeared that the Interstate Realty Company brought a suit in the Federal District Court for the State of Mississippi for the purpose of recovering a broker's commission alleged to be due for the sale of real estate of the defendant in the State of Mississippi.

The suit was based on diversity of citizenship. The Interstate Realty Company, a foreign corporation, had failed to qualify under the laws of the State of Mississippi. The Federal District Court dismissed the complaint with prejudice on the ground that the contract on which the suit was based was void under the law of Mississippi because the plaintiff corporation had failed to qualify in Mississippi. On appeal to the Circuit Court of Appeals, 168 F. 2d 701, 170 F. 2d 694, the judgment of the trial court was reversed, whereupon the defendant carried the case to the Supreme Court of the United States, which reversed the Circuit Court of Appeals. In doing so, the Supreme Court of the United States said:

> "The case is here on a petition for writ of certiorari which we granted because of the seeming conflict of that holding with our recent ruling in Angel v. Bullington, 330 U.S. 183, 67 S. Ct. 657, 91 L. Ed. 832.
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> "If the Lupton's Sons case controls, it is clear that the Court of Appeals was right in allowing the action to be maintained in the federal court. In that case a New York statute provided that no foreign corporation could 'maintain any action in this state' without a certificate that it had qualified to do business there. The Court held that a contract on which the corporation could not sue in the courts of New York by reason of that statute nevertheless could be enforced in the federal court in a diversity suit. The Court said, 225 U.S. at page 500, 32 S. Ct. at page 714, 56 L. Ed. 1177, Ann. Cas. 1914A, 699, 'The state could not prescribe the qualifications of suitors in the courts of the United States, and could not deprive of their privileges those who were entitled under the Constitution and laws of the United States to resort to the Federal courts for the enforcement of a valid contract.'
>
> "We said in Angel v. Bullington that the case of Lupton's Sons had become 'obsolete' insofar as it was 'based on a view of diversity jurisdiction which came to an end with Erie Railroad Co. v. Tompkins, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A.L.R. 1487.' 330 U.S. at page 192, 67 S. Ct. at page 662, 91 L. Ed. 832. Bullington had sued Angel in a North Carolina court for a deficiency judgment on the sale of realty under a deed of trust. The Supreme Court of North Carolina dismissed the action because of a North Carolina statute which disallowed a deficiency judgment in such a case and which the North Carolina Supreme Court construed to be 'a limitation of the jurisdiction of the courts of this state.'

Bullington v. Angel, 220 N.C. 18, 16 S.E. 2d 411, 412, 136 A.L.R. 1054. Thereafter Bullington sued in the federal court of North Carolina by reason of diversity of citizenship. We held that that suit could not be maintained because (1) the prior suit was res judicata; and (2) the policy of Erie R. Co. v. Tompkins precluded maintenance in the federal court in diversity cases of suits to which the State had closed its courts.

"The Court of Appeals concluded that the latter reason was argumentatory, the real basis of the decision being that Bullington was denied recovery on the doctrine of res judicata. But where a decision rests on two or more grounds, none can be relegated to the category of obiter dictum. United States v. Title Ins. & Trust Co., 265 U.S. 472, 486, 44 S. Ct. 621, 623, 68 L. Ed. 1110; Commonwealth of Massachusetts v. United States, 333 U.S. 611, 623, 68 S. Ct. 747, 754, 755, 92 L. Ed. 968.

"Angel v. Bullington in its alternative ground followed the view of Guaranty Trust Co. of New York v. York, 326 U.S. 99, 108, 65 S. Ct. 1464, 1469, 89 L. Ed. 2079, 160 A.L.R. 1231, that for purposes of diversity jurisdiction a federal court is 'in effect, only another court of the State. * * *.' In that case we required the federal court in a diversity case to apply the statute of limitations of the State in equity actions and thus to follow local law, as had previously been done in cases involving burden of proof, Cities Service Oil Co. v. Dunlap, 308 U.S. 208, 60 S. Ct. 201, 84 L. Ed. 196; of Stoner v. New York Life Ins. Co., 311 U.S. 464, 61 S. Ct. 336, 85 L. Ed. 284; contributory negligence, Palmer v. Hoffman, 318 U.S. 109, 117, 63 S. Ct. 477, 482, 87 L. Ed. 645, 144 A.L.R. 719; conflict of laws, Klaxon Co. v Stentor Electric Mfg. Co., 313 U.S. 487, 61 S. Ct. 1020, 85 L. Ed. 1477; Griffin v. McCoach, 313 U.S. 498, 61 S. Ct. 1023, 85 L. Ed. 1481, 134 A.L.R. 1462; and accrual of the cause of action, West v. American Tel. & Tel. Co., 311 U.S. 223, 61 S. Ct. 179, 85 L. Ed. 139, 132 A.L.R. 956. The York case was premised on the theory that a right which local law creates but which it does not supply with a remedy is no right at all for purposes of enforcement in a federal court in a diversity case; that where in such cases one is barred from recovery in the state court, he should likewise be barred in the federal court. The contrary result would create discriminations against citizens of the State in favor of those authorized to invoke the diversity jurisdiction of the federal courts. It was that element of discrimination that Erie R. Co. v. Tompkins was designed to eliminate." (Underscoring added.)

The principle involved in the holding in this case is as applicable to cooperative corporations as it is to a corporation of any other type or character. Any cooperative corporation engaged in intra-State business in any State other than that in which it was incorporated should carefully comply with all the statutes of that State with respect to foreign corporations. Failure to comply with the laws of a State relative to foreign corporations usually means that a foreign corporation may not maintain a suit in the courts of that State.

In Tennessee the shareholders of a foreign corporation that had failed to qualify in that State were held liable as partners. 1/ In Colorado, the officers and agents of a foreign corporation that had failed to qualify under the laws of the State of Colorado were held personally liable. 2/

For other cases bearing on the general subject under consideration, see "Nonprofit Associations" on page 166 of "Legal Phases of Cooperative Associations," and "Associations and Third Persons" on page 289 of the same book.

1/ Cunningham v. Shelby, 136 Tenn. 176, 188 S.W. 1147, L.R.A. 1917B 572.
2/ Fritts v. Palmer, 132 U.S. 282, 10 S. Ct. 93, 33 L. Ed. 317.

In the case of Farmers Reservoir & Irrigation Company v. McComb, 69 S. Ct. 1274, the question for decision was whether the employees of that company were exempt from the provisions of the Fair Labor Standards Act on the ground that they were engaged in agriculture. The company was organized by farmers for the purpose of obtaining a supply of water for the irrigation of their farms. It did not engage in the sale of water. It distributed water only to its own stockholders, each of whom was entitled to a limited amount for each share of stock held. There were no profits and no dividends. "The income of the company is derived largely from assessments levied on the stockholders annually to pay for the costs of operating the system."

Under the terms of the Fair Labor Standards Act, all persons engaged in agriculture are exempt therefrom. 1/ The Supreme Court of the United States held that all the employees of the company were under the Fair Labor Standards Act and that none of them were engaged in agriculture.

In brief, the Court held that the mutual irrigation company, although owned and operated by farmers for the purpose of supplying their farms with water needed for agricultural purposes, constituted a business entity or activity that was separate and apart from the operation of the farms. The following quotations from the opinion show the basis thereof:

> "The District Court held that the field employees were engaged in the production of goods for commerce, as those terms are defined in sec. 3 of the Act, but that the bookkeeper was not. It held, however, that all of the company's employees were exempt under sec. 13(a) (6) as persons 'employed in agriculture.' This second holding was reversed, as to the field employees, by the Court of Appeals for the Tenth Circuit, one judge dissenting, and, in No. 128, we granted the company's petition for certiorari on the exemption issue. The Court of Appeals did not pass on the bookkeeper's status. It regarded his case as moot because his salary was said by the company, in its brief, to have been raised to $210 per month while the appeal was pending. The court regarded this as sufficient to establish his exemption as an administrative employee under sec. 13 (a) (1) of the Act and therefore limited its consideration and its reversal of the District Court to the field employees. In No. 196, we granted the Administrator's cross-petition with respect to the bookkeeper.
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> "It is conceded here that the courts below were correct in holding that the field employees are engaged in the production of goods for commerce. The petitioner, however, argues that this requires the conclusion that they are employed in agriculture. This argument rests on the fact that the activities of the company and its employees

1/ 29 U.S.C. 201, 213

are entirely confined within the State of Colorado. The company diverts water in Colorado, stores it in Colorado, distributes it in Colorado to farmers who, finally, consume it in Colorado. The only products moving in interstate commerce are the agricultural commodities produced by the farmers who consume the company's water. Hence, it is said that we can hold that the company's employees are engaged in the production of goods for interstate commerce only if we say that their work in supplying water to the farmers is an integral part of the production of the farm products which are shipped in interstate commerce. But that production is, of course agriculture. Hence, the company's employees, if they are engaged in the production of goods for commerce, must be exempt as persons employed in agriculture.

"The argument rests on a misconstruction of sec. 3(j) of the Fair Labor Standards Act--the section which the courts below relied on in concluding that the field employees of the company are engaged in the production of goods for commerce. Section 3(j) provides that 'for purposes of this Act an employee shall be deemed to have been engaged in the production of goods if such employee was employed * * * in <u>any process or occupation necessary to the</u> production thereof.' From the beginning, this Court has refused either to read this provision out of the Act by limiting the coverage of the Act to those actually engaged in production or, on the other hand, to expand it so as to include every process or occupation affecting production for commerce. We have held that if an occupation, not itself production for commerce, has 'a close and immediate tie' with the process of production, it comes within the provisions of sec. 3(j). Applying this standard, the Court of Appeals quite properly held that the field employees here are engaged in an occupation necessary, in the statutory sense, for the production of agricultural commodities shipped in commerce.

"But the conclusion that the work <u>is necessary</u> to agricultural production does not require us to say that it <u>is</u> agricultural production. This distinction between necessity and identity, or, differently phrased, between production in the normal sense and production in the special sense defined in sec. 3(j) disposes of the petitioner's contention. The question here is whether the occupation of the field employees of the ditch company can itself be termed agriculture. The answer to that question is not predetermined by the fact that the occupation is within the scope of the Act because it has a necessary connection, in commerce, with agricultural production.

"Agriculture, as an occupation, includes more than the elemental process of planting, growing and harvesting crops. There are a host of incidental activities which are necessary to that process. <u>Whether a particular type of activity is agricultural depends, in large measure, upon the way in which that activity is organized in a particular society.</u> The determination cannot be made in the abstract. <u>In less advanced societies the agricultural function includes many types of activity which, in others, are not agricultural.</u> The fashioning of tools, the provision of fertilizer, the processing of the product, to mention only a few examples, are functions which, in some societies, are

performed on the farm by farmers as part of their normal agricultural routine. Economic progress, however, is characterized by a progressive division of labor and separation of function. Tools are made by a tool manufacturer, who specializes in that kind of work and supplies them to the farmer. The compost heap is replaced by factory produced fertilizers. Power is derived from electricity and gasoline rather than supplied by the farmer's mules. Wheat is ground at the mill. In this way functions which are necessary to the total economic process of supplying an agricultural product, become, in the process of economic development and specialization, separate and independent productive functions operated in conjunction with the agricultural function but no longer a part of it. Thus, the question as to whether a particular type of activity is agricultural is not determined by the necessity of the activity to agriculture nor by the physical similarity of the activity to that done by farmers in other situations. The question is whether the activity in the particular case is carried on as part of the agricultural function or is separately organized as an independent productive activity.. The farmhand who cares for the farmer's mules or prepares his fertilizer is engaged in agriculture. But the maintenance man in a power plant and the packer in a fertilizer factory are not employed in agriculture, even if their activity is necessary to farmers and replaces work previously done by farmers. The production of power and the manufacture of fertilizer are independent productive functions, not agriculture. (Underscoring added.)

"In the absence of a detailed definition of agriculture we should be compelled to determine whether the activity concerned in the present case--the diversion, storage and distribution of water for irrigation purposes--is carried on as part of the agricultural function or is so separately organized and conducted as to be treated as an independent, nonagricultural productive function. Fortunately, however, the Fair Labor Standards Act provides a carefully considered definition which is of substantial aid in helping us to make that determination.

"The definition is contained in sec. 3(f) of the Fair Labor Standards Act. It says:

"'Sec. 3(f). "Agriculture" includes farming in all its branches and among other things includes the cultivation and tillage of the soil, dairying, the production, cultivation, growing, and harvesting of any agricultural or horticultural commodities (including commodities defined as agricultural commodities in section 15(g) of the Agricultural Marketing Act, as amended), the raising of livestock, bees, furbearing animals, or poultry, and any practices (including any forestry or lumbering operations) performed by a farmer or on a farm as an incident to or in conjunction with such farming operations, including preparation for market, delivery to storage or to market or to carriers for transportation to market.'

"As can be readily seen this definition has two distinct branches. First, there is the primary meaning. Agriculture includes farming in all its branches. Certain specific practices such as cultivation and tillage of the soil, dairying, etc., are listed as being included

in this primary meaning. Second, there is the broader meaning. Agriculture is defined to include things other than farming as so illustrated. It includes any practices, whether or not themselves farming practices, which are performed either by a farmer or on a farm, incidently to or in conjunction with 'such' farming operations.

"Dealing with these two branches of the definition in order it is clear, first, that the occupation in which the petitioner's employees are engaged is not farming. The petitioner owns no farms and raises no crops. Irrigation, strictly defined--that is the actual watering of the soil--may no doubt be called farming. And the work of the farmers in seeing to it that the water released from the company's ditches is properly distributed to the growing plants undoubtedly is included in farming as being part of the process of cultivating and tilling the soil. But the significant fact in this case is that this work is not done by the company's employees. There is a clear and definite division of function. The ditch company carries the water in its own canals to the lands of the farmers. When a farmer desires water so that he can irrigate his fields he notifies the company. Its employees then operate the headgates, which are located on the company's canals and which the farmers are forbidden to operate, so that the appropriate quantity of water can pass out of the company's canals and off the company's land into the farmer's irrigation ditches. The responsibility of the company's employees ceases when they so release the water. The water is supplied to the farmer at the headgates and he takes it over there and uses it, in his own laterals, as he sees fit, to irrigate his crops.

"The ditch company, then, is not engaged in cultivating or tilling the soil or in growing any agricultural commodity. It is contended, however, that it is nevertheless engaged in farming because of the use, in the definition, of the words 'production * * * of any agricultural * * * commodities' in addition to the words cultivation, tillage, harvesting, etc. Since produce is defined in sec. 3(j) of the Act so as to include, 'for the purposes of this Act,' any occupation necessary to production, it is argued that production of agricultural commodities includes any occupation necessary to the production of agricultural commodities. It is thus argued that in the case of agriculture, as distinguished from other exemptions, Congress did provide that the exemption should include not only the occupation named but also all of those other occupations whose work is necessary to it.

"If Congress intended to convey that meaning by using the word production in the definition of agriculture we should, of course, give the definition its intended scope. But we do not 'make a fortress ouf of the dictionary.' And we have, therefore, consistently refused to pervert the process of interpretation by mechanically applying definitions in unintended contexts. Lawson v. Suwanee Fruit & S.S. Co., 1949, 336 U.S. 198, 69 S. Ct. 503; Atlantic Cleaners & Dyers v. United States, 1932, 286 U.S. 427, 52 S. Ct. 607, 76 L. Ed. 1204. In the present case, the legislative history confirms what a natural

reading of the language of the agricultural exemption would indicate--the word production was not there used in the artificial and special sense in which it was defined in sec. 3(j). Certainly, if it were meant in that sense, it would make surplusage of the remainder of the carefully wrought definition. And it would hardly have been innocuously placed among such specific terms as 'cultivation,' 'tillage,' 'growing,' and 'harvesting.'

"But we need not speculate on the congressional meaning. The history of the use of the word production is crystal clear. It was added to the definition of agriculture in order to take care of a special situation--the production of turpentine and gum rosins by a process involving the tapping of living trees. There had been indications that such activity would not be considered agriculture, since turpentine is neither cultivated nor grown. And a special amendment, sec. 15(g), had been added to the Agricultural Marketing Act specifying that commodities so produced were to be considered agricultural commodities for the purposes of that Act. To insure the inclusion of the process within the agricultural exemption of the Fair Labor Standards Act, the word production was added to sec. 3(f) in conjunction with the words 'including commodities defined as agricultural commodities in sec. 15(g) of the Agricultural Marketing Act as amended.'

"It is unnecessary to decide whether, in view of this history, the word production in the agricultural exemption should be limited to those specific products defined in sec. 15(g) of the Agricultural Marketing Act or should be given its normal meaning. The only question here is whether the word was used in the special expanded meaning defined in sec. 3(j) of the present Act. It is clear that it was not used in this special sense. And it follows that it does not encompass the work of the petitioner's employees who cannot be said, in any normal use of the term, to be engaged in the production of agricultural commodities. Their work is necessary to agricultural production, but it is not production.

"The work of the petitioner's employees is not, then, farming. But, coming to the second branch of the definition of agriculture, it is equally clear that it does constitute a practice performed as an incident to or in conjunction with farming. If the Act exempted all such practices the company would be exempt. But the exemption is limited. <u>Such practices are exempt only if they are performed by a farmer or on a farm.</u>" (Underscoring added.)

Mr. Justice Jackson dissented, and the following quotation is taken from his dissenting opinion:

"This irrigation seems to me to be 'performed by a farmer' and hence, by definition, part of the operation of agriculture. <u>Certainly the agricultural exemption is not lost because farmers pool their capital through a mutual, nonprofit corporation for no other purpose whatever than to carry water to their own arid lands to make it possible to produce crops</u>. The only purpose of the corporate form is to limit

individual liability for a project which is subsidiary to each farmer's main enterprise but which is beyond the means or demands of any of them as individuals. Only the landowners can become stockholders; only the stockholders can become water users, and the operating costs and capital charges are met by assessing them in proportion to their water benefits. Employees engaged in the water operation would be on a quite different footing if it were a water company selling water to the public or the farmer for profit." (Underscoring added.)

From the majority opinion in the case, it is clear that if each farmer had individually owned and operated his own irrigation ditches, the workers employed in thus irrigating a farmer's farm would have been engaged in agriculture. But, even though the farmers themselves were engaged in obtaining water for the irrigation of their farms through the medium of a mutually owned and operated irrigation company, the Court was of the opinion that the employees of the mutual irrigation company were not engaged in agriculture, and were not engaged in the performing of work on a farm, and hence were not exempt as engaged in agriculture under the Fair Labor Standards Act. Of course, it is to be remembered that the decision of the Court rests largely, if not entirely, on the definition of agriculture as given in the Fair Labor Standards Act, and of course if Congress had included a broader definition of agriculture, it might have included employees of a mutual irrigation company.

For other cases bearing on the principle involved in the instant case, see "Legal Phases of Cooperative Associations," pages 240, 242.

STATE ACTION DID NOT VIOLATE SHERMAN ACT

In 1933, the California Agricultural Prorate Act was enacted by that State. This Act gave officials of the State of California authority to adopt programs with reference to an agricultural commodity under which the marketing and handling of any such commodity would be under the control of officials of the State. In pursuance of authority conferred by this California statute, a marketing program was adopted by the State of California for the 1940 raisin crop. It seems to have been admitted that one of the immediate results of the adoption of this raisin program was to increase the price of raisins by $10 per ton. Porter L. Brown brought an action against W. B. Parker, Director of Agriculture, Agricultural Prorate Advisory Commission, Raisin Proration Zone No. 1, and others, to restrain enforcement as to plaintiff of the prorate plan for raisins. Before a three-judge Federal District Court, the plaintiff prevailed (39 F. Supp. 895), and the defendant then appealed to the Supreme Court of the United States (Parker v. Brown, 317 U.S. 341), which reversed the ruling of the trial court and held that the raisin program was legal. The Supreme Court stated:

> "The questions for our consideration are whether the marketing program adopted for the 1940 raisin crop under the California Agricultural Prorate Act is rendered invalid (1) by the Sherman Act, 15 U.S.C.A. sec. 1-7, 15 note, or (2) by the Agricultural Marketing Agreement Act of 1937, as amended, 7 U.S.C. sec. 601 et seq., 7 U.S.C.A. sec. 601 et seq., or (3) by the Commerce Clause of the Constitution, art. 1, sec. 8, cl. 3.
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> "Appellee, a producer and packer of raisins in California, brought this suit in the district court to enjoin appellants--the State Director of Agriculture, Raisin Proration Zone No. 1, the members of the State Agricultural Prorate Advisory Commission and of the Program Committee for Zone No. 1, and others charged by the statute with the administration of the Prorate Act--from enforcing, as to appellee, a program for marketing the 1940 crop of raisins produced in 'Raisin Proration Zone No. 1'. After a trial upon oral testimony, a stipulation of facts and certain exhibits, the district court held that the 1940 raisin marketing program was an illegal interference with and [an] undue burden upon interstate commerce and gave judgment for appellee granting the injuction prayed for. D.C., 39 F. Supp. 895. The case was tried by a district court of three judges and comes here on appeal under secs. 266 and 238 of the Judicial Code as amended, 28 U.S.C. secs. 380, 345, 28 U.S.C.A. secs. 380, 345."
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> "The California Agricultural Prorate Act authorizes the establishment, through action of state officials, of programs for the marketing of agricultural commodities produced in the state, so as to restrict competition among the growers and maintain prices in the distribution of their commodities to packers. The declared purpose of the Act is to 'conserve the agricultural wealth of the State' and to 'prevent economic waste in the marketing of agricultural crops' of the state.

It authorizes, sec. 3, the creation of an Agricultural Prorate Advisory Commission of nine members, of which a state official, the Director of Agriculture, is ex-officio a member. The other eight members are appointed for terms of four years by the Governor and confirmed by the Senate, and are required to take an oath of office. sec.4."

* * * * * *

"Under the program the producer is permitted to sell the remaining 30 percent of his standard raisins, denominated 'free tonnage', through ordinary commercial channels, subject to the requirement that he obtain a 'secondary certificate' authorizing such marketing and pay a certificate fee of $2.50 for each ton covered by the certificate. Certification is stated to be a device for controlling 'the time and volume of movement' of free tonnage into such ordinary commercial channels. Raisins in the stabilization pool are to be disposed of by the committee 'in such manner as to obtain stability in the market and to dispose of such raisins', but no raisins, (other than those subject to special lending or pooling arrangements of the Federal Government) can be sold by the committee at less than the prevailing market price for raisins of the same variety and grade on the date of sale. Under the program the committee is to make advances to producers of from $25 to $27.50 a ton, depending upon the variety of raisins, for deliveries into the surplus pool, and from $50 to $55 a ton for deliveries into the stablization pool. The committee is authorized to pledge the raisins held in those pools in order to secure funds to finance pool operations and make advances to growers."

In showing that the California Agricultural Prorate Act and the program with respect to raisins adopted thereunder did not violate the Sherman Act, the Court said:

"But it is plain that the prorate program here was never intended to operate by force of individual agreement or combination. <u>It derived its authority and its efficacy from the legislative command of the state and was not intended to operate or become effective without that command. We find nothing in the language of the Sherman Act or in its history which suggests that its purpose was to restrain a State or its officers or agents from activities directed by its legislature</u>. In a dual system of government in which, under the Constitution, the States are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress." (Underscoring added.)

* * * * * *

"The state in adopting and enforcing the prorate program <u>made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not</u>

undertake to prohibit. Olsen v. Smith, 195 U.S. 332, 344, 345, 25 S. Ct. 52, 54, 55, 49 L. Ed. 224; cf. Lowenstein v. Evans, C.C., 69 F. 908, 910." (Underscoring added.)

It was also claimed that the California statute and the action taken thereunder violated the Federal Agricultural Marketing Agreement Act. The Court, however, found that no Federal program with respect to raisins had been adopted under the Agricultural Marketing Agreement Act, and that action taken by the United States Department of Agriculture was consistent with approval of the program in regard to raisins that was being carried out by the State of California. After giving a resume of the history of the raisin industry in California, the Court said:

> "This history shows clearly enough that the adoption of legislative measures to prevent the demoralization of the industry by stabilizing the marketing of the raisin crop is a matter of state as well as national concern and, in the absence of inconsistent Congressional action, is a problem whose solution is peculiarly within the province of the State. In the exercise of its power the state has adopted a measure appropriate to the end sought. The program was not aimed at nor did it discriminate against interstate commerce, although it undoubtedly affected the commerce by increasing the interstate price of raisins and curtailing interstate shipments to some undetermined extent. The effect on the commerce is not greater, and in some instances was far less, than that which this Court has held not to afford a basis for denying to the states the right to pursue a legitimate state end. Cf. Kidd v. Pearson, supra; Sligh v. Kirkwood, supra; Champlain Refining Co. v. Corporation Commission, supra; South Carolina State Highway Department v. Barnwell Bros., supra, and cases cited at page 189, of 303 U.S., at page 516 of 58 S. Ct., 82 L. Ed. 734, and notes 4 and 5; People of State of California v. Thompson, supra, 313 U.S. 113, 115, 61 S. Ct. 932, 933, 85 L. Ed. 1219, and cases cited." (Underscoring added.)

The case under discussion seems to clearly indicate that a state in the absence of Federal action that is inconsistent therewith may take reasonable steps that are intended to regulate and control the marketing and handling of an agricultural commodity produced within that state. As shown in the opinion, the Sherman Act is in no way violated by any such action as long as the action in question is state action as distinguished from private or individual action. The opinion points out that a State could not abrogate the Sherman Act by attempting to authorize individuals to take action that was inconsistent therewith.

For other cases involving the principles analagous to those reflected in the case under discussion, see Milk Board v. Eisenberg Co., 306 U.S. 346; H. P. Hood & Sons, Inc., v. Du Mond, 297 N.Y. 209, 78 N.E. 2d 476; but see H. P. Hood & Sons, Inc., v. Du Mond, 336 U.S. 525.